

FOCAL POINT

German fiscal bazooka: Just a flash in the pan?

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Our Focal Point series explores topical issues on macro, markets and investment

- Last year's German 'fiscal bazooka' announcement of almost € 1 tr of additional infrastructure and defence spending until 2030, may boost growth by on average 0.2 to 0.4 pp annually over the coming years.
- In practice, the specific budget plans, esp. the one on infrastructure, add to expenditures and debt but little to public investment. Up to 40–49% of the funds are re-routed to government consumption as quotas are distorted and spending shifted across budgets thereby reducing the macro gains.
- The EC endorsed the German budget in autumn 2025 but if the expected boost to growth fades quickly and debt sustainability deteriorates there will also be conflicts with the European fiscal rules further down the road.
- So far additional spending has not shown up in hard production data but rising industrial orders are encouraging. The 2026 fiscal impulse of 1.2 pp suggests a growth push in the 0.3 pp to 0.8 pp range and will help to lift German growth from 0.3% in 2025 to 1.2% in 2026.
- To lift growth lastingly a proper use of the bazooka amid substantial reforms (e.g. less bureaucracy, improve competitiveness) are of essence. Otherwise, the German bazooka will in the end only be a flash in the pan.

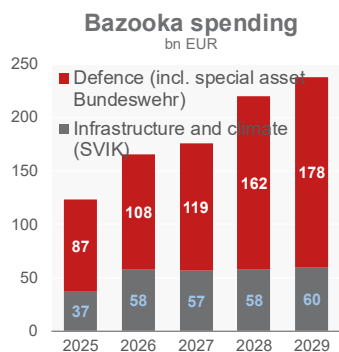
Following the snap election in early 2025, Germany's conservative Chancellor Merz executed a sharp fiscal U-turn. Prompted by the sudden withdrawal of US aid to Ukraine and the need to form a coalition with the Social Democrats, he pushed through a reform of the debt brake and a €500 bn infrastructure and climate fund. Markets and analysts turned more optimistic, and expectations of growth-enhancing reforms led some to predict a strong upswing, with the 2026 growth forecast rising to about 1.3% in April 2025 (Bloomberg consensus). Since then, however, reform momentum has disappointed, and the 2026 budget plans have reinforced criticism that much of the unprecedented "fiscal bazooka" will merely plug budget gaps. While we share this criticism, we nevertheless expect a strong activity boost in 2026.

Fiscal bazooka to potentially amount to almost € 1 tr until 2030

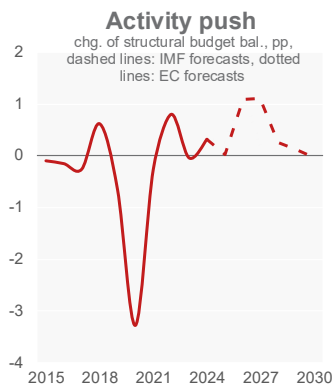
After protracted negotiations, three centrist parties of the outgoing German parliament (CDU/CSU, SPD and Greens) agreed on 18 March 2025 on a landmark reform of the debt brake and the creation of a major infrastructure and climate fund. First, all defense spending above 1% of GDP will be exempt from the debt brake, corresponding to about €44 bn based on 2024 nominal GDP. Second, the Länder will no longer be required to run balanced budgets and may incur annual borrowing of up to 0.35% of GDP, or roughly €15 bn. Third, a €500 bn special fund for infrastructure and climate neutrality (SVIK) will be established over twelve years. Of this, €100 bn is earmarked for the Länder.

Assuming Germany meets the new [NATO](#) defense target of 3.5% of GDP, defense spending will rise sharply in 2026, reflecting both the additional fiscal leeway and the existing special fund ([Sondervermögen Bundeswehr](#)). Also, expenses for the SVIK will increase significantly in 2026. These increases will amount to € 44 bn or about 1% of German GDP. In the coming years this fiscal impulse flattens but clearly stays supportive. This pattern remains unchanged when considering the ‘normal budget’ items.

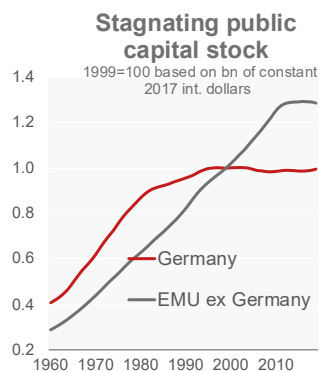
Total additional spending over the medium term depends on whether the defense special fund (€126 bn for 2025–29) is fully included. Based on current planning by the Ministries of Finance and Defense, cumulative spending in 2025–29 would amount to €580–700 bn, with upside risks if the 3.5% defense target is reached earlier than planned. Adding the Länder’s borrowing leeway – assumed to be fully used (€91 bn) – total fiscal expansion could reach around €1 trillion by 2030.



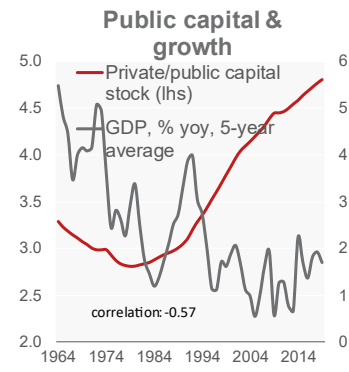
Sources: [German Ministry of Defence](#), [German Ministry of Finance](#)



Source: Datastream, GenAM



Source: IMF Investment and Capital Stock Dataset, 2021, GenAM



Source: Datastream, IMF Investment and Capital Stock Dataset, 2021, GenAM

Strong potential growth effects

The potential growth effects are substantial, particularly as Germany’s public capital stock has stagnated, constraining growth (see rhs graphs). The sizeable public [infrastructure investment gap](#) – estimated at around €600 bn – could be significantly reduced, if not fully closed. The package enables private firms, such as construction companies, to invest in the required capacity and provides defense contractors with a stable demand outlook. Simulations of these “bazooka effects” point to meaningful growth gains in 2026–2030: the European Commission’s [Quest model](#) model estimates an annual boost of 0.2–0.4 pp, while some market participants are more optimistic – [Goldman Sachs](#), for example, upgrades medium-term growth by roughly 0.4–0.6 pp relative to pre-reform expectations.

... but loopholes will diminish its effectiveness

While there is broad agreement on the sizeable growth potential, skepticism remains over whether the funds will be used effectively or merely serve as an additional budgetary backstop. In particular, the SVIK is criticized for delivering limited genuinely additional, growth-enhancing investment while adding substantial debt.

First, the principle of additionality is systematically diluted. The [IW](#) estimates that 2025–2029, 40–49% of the new debt does not finance additional investment (up to € 133 bn), with even optimistic benchmarks implying around 26% non-additional use. The [German Council of Economic Experts](#) (SVR 2025, chapter 2) likewise gauges very low additionality ($\approx 8\%$ in 2025, $\approx 45\%$ in 2026; 50% thereafter). Second, the statutory 10% investment quota for the normal budget that shall prevent merely outsourcing investment activity to the supplementary budgets is weak and methodologically distorted (IW): it counts defense investment in the numerator while excluding it from the denominator, inflating the ratio by $\sim 0.5\text{pp}$ ($\sim \text{€}2.3\text{bn}$). Plan values, not outturns, further mask persistent under-execution and carry-overs of $\text{€}17\text{--}20\text{bn}$ p.a. (SVR).

Third, a ‘shell game’ shifts items between the core budget and the SVIK. Relative to the prior plan, federal core-budget investment drops by $\text{€} 92.6$ bn (2025–2028), while SVIK replenishes (SVR). Fourth, reported ‘investment’ contains large volumes of loans, guarantees and carry-over provisions; classic construction/infrastructure has a shrinking share in the core budget ([ifo](#)). Fifth, transparency and governance are weak – titles are re-labelled or double-counted, and monitoring lacks binding powers (SVR).

Sixth, Länder/municipal rules are too loose: 40% of SVIK resources face no strict additionality (SVR, IW), and municipalities ran a $\text{€} 24.8$ bn deficit in 2024; the SVR recommends a 60–70% pass-through to municipalities and moderate co-financing with safeguards. Seventh, macroeconomic effects are modest in the current policy path: by 2030, $\text{€} 426$ bn (real) of extra spending yields only $\sim \text{€} 246$ bn of extra GDP; an investment-heavy path would perform better (SVR). Eighth, defense ‘exemption’ practices distort the investment ratio and raise debt without commensurate growth (SVR). Ninth, specific accounting choices (e.g., counting defense, shifting coal-region subsidies while moving transport/broadband to SPV) are formally compliant but economically weak (IW).

European fiscal rules a medium-term constraint

Against these shortcomings we agree with ifo’s conclusion that the 2026 core budget underscores the trend: more debt reliance, fewer genuine infrastructure items, and continued off-budget outsourcing. Medium term this will not only deteriorate the country’s debt trajectory but also risk a clash with the EU fiscal rules. The key feature of the [reformed SGP](#) is a country-specific net expenditure path based on debt-sustainability analysis, the continued 3% deficit reference and 60% debt benchmark (Treaty-level), Medium-Term Fiscal-Structural Plans (MTFSPs) covering 4–5 years, extendable to up to 7 years with reforms/investment and Surveillance over general government, including off-budget funds like the German SVIK.

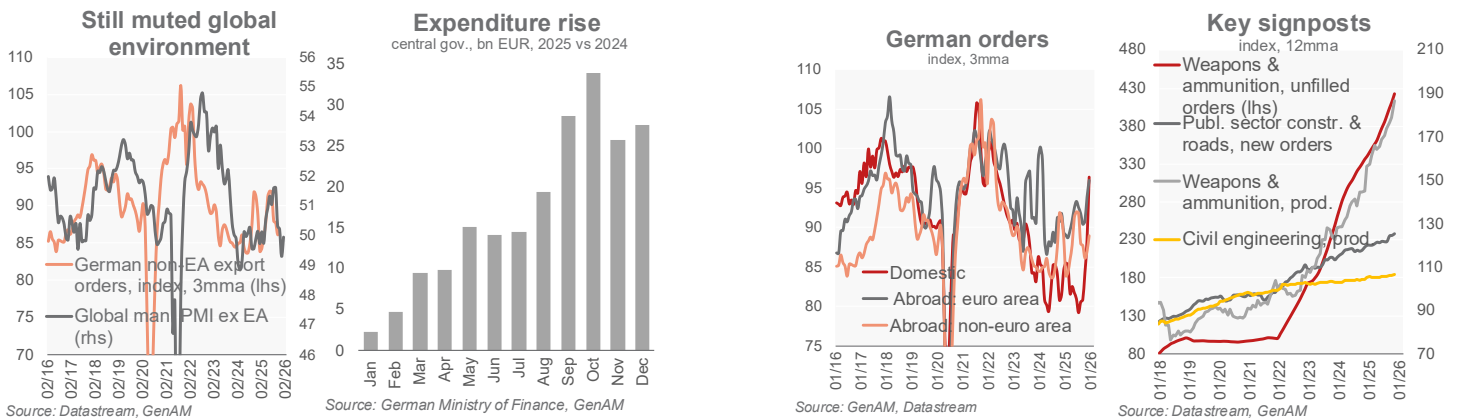
However, the [EC](#) endorsed Germany’s fiscal package considering that its debt ratio (of 63% in 2025) is only slightly above the 60% threshold, it currently is a low-risk country regarding debt sustainability and this allows gradual and back-loaded adjustment path. That said, the SVR and a study by [Bruegel](#) show that the full use of the fiscal space granted in the long run by the reformed national debt brake is inconsistent with EU debt

rules causing the debt ratio to potentially rise towards 90% to 100%. With proper use of the bazooka money we see the debt ratio rising to around 70% by 2030 and find this number stretched. But clearly, the less investment and hence productivity enhancing the bazooka money is used, the sooner a clash with European fiscal rules might emerge.

Nevertheless, huge fiscal impulse to trigger a recovery in 2026

While the full growth-enhancing potential of the fiscal bazooka is unlikely to be realised, the 2026 budget implies a strong fiscal impulse that should materially support activity. As the economy continues to face multiple headwinds – de-globalisation, high energy prices and intensifying global competition – industrial production has stabilised at low levels and still lags European peers. At the start of 2026, the composite PMI has recovered only to its November level and remains close to its historical norm, while the ifo index is still well below average. After three recessionary years, spare capacity is substantial: the 2026 output gap is clearly negative, ranging from -0.9% (IMF) to -2.0% (Oxford Economics). Capacity utilisation stands at 78% in industry (vs. 83% average) and 67% in construction, about 9 pp below normal. Against this backdrop, we expect the 1.2 pp fiscal impulse to deliver a strong boost to growth. With fiscal multipliers estimated between 0.3 and 0.7 (e.g. see [here](#) or [here](#)), this implies an additional 0.4–0.8 pp of growth; given the large output gap and low utilisation in stimulus-targeted sectors, we expect the multiplier to be at the upper end.

The stimulus is already in the pipeline. Central government spending has risen sharply since September 2025, up €116 bn (+7.5%) year on year. SVIK [spending reached € 24 bn](#) in 2025, below the planned €37 bn, but is expected to be caught up alongside the



€58 bn scheduled for 2026. Domestic industrial orders are increasing (+7.9% mom in Dec); while partly driven by catch-up investment and one-off effects, they are also supported by bazooka-related spending, notably defense procurement and infrastructure and rail investment. Domestic orders (+10.7% mom in Dec) jumped to a level not seen since July 2021. Likewise, public construction orders are rising and should translate into stronger output. Q4 2025 GDP surprised on the upside (+0.3% qoq), supported by both household and government consumption. Overall, clear signs suggest the fiscal bazooka is gaining traction. Assuming current momentum is maintained and accelerates with fiscal support, we see 2026 GDP growth of 1.2%, slightly above the 1.1% consensus. That said, sustained growth will require effective use of the funds alongside structural reforms – such as reducing bureaucracy and improving external competitiveness – otherwise the bazooka risks proving only a flash in the pan.

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